July 14, 2017

VIA EMAIL pubcom@finra.org

Jennifer Piorko Mitchell
Office of the Corporate Secretary
FINRA
1735 K Street, NW
Washington, DC 20006-1506

Re: FINRA's Regulatory Notice 17-14 ("RN 17-14") request for comments regarding FINRA Rules Impacting Capital Formation

Dear Ms. Piorko Mitchell:

The Investment Program Association ("IPA") respectfully submits this letter in response to the request for comments by the Financial Industry Regulatory Authority ("FINRA") on RN 17-14 (regarding FINRA rules impacting capital formation). Our intent is to provide comments we believe will improve the information provided to investors to assist them with decision making in regards to asset classes and investment strategy. The IPA is the leading advocate for the inclusion of direct investment products in a diversified portfolio, including non-listed REITs, non-listed business development companies, private equity real estate and energy and equipment leasing programs.

FINRA'S REQUEST:

FINRA recently announced a new initiative—called FINRA360—to evaluate various aspects of its operations and programs to identify opportunities to more effectively further its mission. As part of this initiative, FINRA is requesting comment on the effectiveness and efficiency of its rules, operations and administrative processes governing broker-dealer activities related to the capital-raising process and their impact on capital formation.

IPA'S PROPOSALS:

The IPA appreciates FINRA's proactive consideration of the suggestions to improve the effectiveness and efficiency of its rules, operations and administrative processes governing broker-dealer activities related to the capital-raising process and their impact on capital formation. We would like propose the following points for FINRA's consideration and welcome an opportunity to work together to develop appropriate investor and industry solutions.

1. FINRA rules currently require a detailed itemized submission of estimated underwriting compensation and organizational and offering expenses for public offerings by direct participation programs ("DPP").[1] This information is typically submitted to FINRA by the managing broker-dealer for the public offering. The IPA proposes revisions to FINRA's procedures related to such review and revisions to the applicable FINRA rules to require substantially less information be submitted to FINRA and instead include a representation by managing broker-dealers that (a) underwriting compensation will not exceed 10% of offering proceeds (excluding proceeds from the sale of securities purchased through the reinvestment of dividends ("DRP Proceeds")) at the completion of the offering and (b) organization and offering expenses will not exceed 15% of gross offering proceeds.[2] The current process takes managing broker-dealers and DPPs significant costs and time to produce the required information and respond to comments from FINRA staff. Simplifying the submission and review process will reduce of some of these costs and time. This will ease the burden on market participants, including new entrants, which will help facilitate new capital raising and increase investor returns because of the resulting lower up-front costs.

2. The IPA would like to discuss with FINRA potential relief from penalties and required procedures when DPPs exceed the 10% cap on underwriting compensation due to (a) the premature termination of the offering; (b) the inability to raise sufficient capital to "grow" out of the high up-front offering costs; (c) the merger of the DPP into another entity; or (d) another situation that causes the early termination of the offering. We suggest that a managing broker-dealer have the ability to submit its costs incurred to FINRA, and if those costs are fair and reasonable under the circumstances, no "repayment" of any overage above the 10% cap to the DPP would be required. "Repayment" by the sponsor or managing broker-dealer of costs in excess of the 10% cap typically results in a windfall to the DPP if the costs were originally paid by the sponsor or managing broker-dealer and not reimbursed with offering proceeds. The reason for the 10% cap on underwriting compensation was to limit unfair and unreasonable compensation, but due to high up-front costs required when an offering begins to introduce a new offering to broker-dealers before any sales begin, cases may exist where an early termination of an offering may cause amounts to be higher than the 10% cap due to no fault of or excessive spending by the managing broker-dealer. The ultimate question to be clarified is who should bear the cost overage when up-front costs are fair and reasonable under the circumstances but still exceed the cap. Requiring the sponsor or managing broker-dealer to "repay" overages to the DPP does not serve to protect the

[1] FINRA Rule 5110(b)(1).

[2] FINRA Rule 2310(b)(4)(B)(i)-(ii).

investor and creates regulatory uncertainty that serves as a disincentive for new participants to enter the market, thereby hindering capital formation.

3. FINRA Rules require that for discretionary accounts, the financial advisor must have prior written approval from the client before the financial advisor can complete the purchase of an investment in a DPP.[3] Despite having a valid power of attorney or full discretion over their client's accounts, this rule prevents registered investment advisers or other financial advisors with discretion to invest in DPPs and sign subscription agreements on behalf of their clients. We request that FINRA either eliminate the provisions of Rule 2310(b)(2)(c) or add language exempting from the rule situations where the client is an accredited investor. Most registered investment advisers that manage significant capital may invest in hedge funds, derivatives or private equity programs on behalf of their clients on a discretionary basis. We do not believe that investments in other alternative investment programs, such as non-listed REITs and business development corporations should be treated differently.

4. With respect to sales charge limitations, the IPA believes that FINRA should take the same approach with continuously offered perpetual-life, publicly offered non-listed REITs ("PLRs") that it takes with open-end investment management companies under the Investment Company Act of 1940, as amended (the "1940 Act") ("Open-End Funds"),[4] certain closed-end management companies ("Closed-End Funds")[5] that make periodic repurchases of their securities under Rule 23c-3(b)[6] of the 1940 Act ("Interval Funds") and offer their shares on a continuous basis pursuant to Rule 415(a)(1)(xi) under the Securities Act of 1933, as amended,[7] and proposes to take with continuously offered

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[3] FINRA Rule 2310(b)(2)(c).

[4] Section 5(a)(1) of the 1940 Act defines "open-end company" as "a management company which is offering for sale or has outstanding any redeemable security for which it is the issuer." 15 U.S.C. 80a-5(a)(1).

[5] Section 5(a)(2) of the 1940 Act defines "closed-end company" as "any management company other than an open-end company." 15 U.S.C. 80a-5(a)(2). While Closed-End Funds are subject to the core provisions of the 1940 Act that also apply to Open-End Funds, including prohibitions on affiliated transactions, obligations requiring stockholder approval of advisory contracts, anti-pyramiding restrictions, and board composition requirements, they are not subject to other 1940 Act restrictions applicable to Open-End Funds, including limitations on leverage and obligations pertaining to the liquidity of investments. *See id.*

[6] 17 CFR 270.23c-3(b).

[7] We note that not all "interval funds" are continuously offered. *See* Securities Exchange Act Release No. 42965 (June 20, 2000); 65 F.R. 39640 (June 27, 2000).

closed-end "tender offer" funds ("Tender Offer Funds")[8] because PLRs are structured in a manner more like Open-End Funds and continuously offered Interval Funds and Tender Offer Funds. Given the similarities between the manner in which PLRs are offered and sold to investors and the means by which PLR investors obtain liquidity for their shares to the manner in which Open-End Funds, continuously offered Interval Funds, and continuously offered Tender Offer Funds are offered and sold and by which their investors obtain liquidity, the IPA believes that the limit on underwriting compensation under FINRA Rule 2310 of 10% of the gross proceeds of an offering (excluding DRP Proceeds), taking into account "the total amount of all items of compensation from whatever source, including compensation paid from offering proceeds and in the form of 'trail commissions,' payable to underwriters, broker-dealers, or affiliates thereof" is inappropriate for PLRs.[9] Rather, we believe that, similar to Open-End Funds and continuously offered Interval Funds, and as proposed for continuously offered Tender Offer Funds, FINRA Rule 2341's requirements that anticipate ongoing asset-based sales charges for continuous offerings, as opposed to a hard cap on the gross proceeds of an offering, would be more appropriate for PLRs. We believe that this change reflects the evolution and modernization of the industry and would assist in capital formation.

The IPA supports FINRA's new initiative, FINRA360 to evaluate various aspects of its operations and programs to identify opportunities to more effectively further its mission. In support of this initiative, the IPA believes these suggestions will improve the information provided to investors to assist them with decision making in regards to asset classes and investment strategy and further stimulate efficient capital formation.

Sincerely,

Anthony Chereso
President & CEO, Investment Program Association

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[8] Tender Offer Funds are closed-end management investment companies that make periodic self-tenders in compliance with Rule 13e-4 and Schedule 13E-4 under the Securities Exchange Act of 1934, as amended.

[9] FINRA Rule 2310(b)(4)(B)(ii).

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